

- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

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In the Matter of the Application for Increase in	)	
USF Eligibility for Carbon/Emery Telecom,	)	DOCKET NO. 05-2302-01
Inc.	)	DPU Exhibit 3.0
	)	
	)	Direct Testimony of
	)	Casey J. Coleman
	)	

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DIVISION OF PUBLIC UTILITIES  
DEPARTMENT OF COMMERCE

November 16, 2005

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1 **I. IDENTIFICATION OF WITNESS**

2 **Q. PLEASE STATE YOUR NAME, EMPLOYER, AND BUSINESS ADDRESS.**

3 A. My name is Casey J. Coleman. I am employed by the Division of Public Utilities for the  
4 State of Utah. My business address is 160 East 300 South Salt Lake City, UT 84114.

5 **Q. BRIEFLY OUTLINE YOUR EMPLOYMENT BACKGROUND.**

6 A. Before working for the Division of Public Utilities for the State of Utah, I was employed  
7 by a telecommunications consulting firm as a Financial Analyst. For approximately the  
8 last five years I have worked for the Division of Public Utilities as a Utility Analyst.

9 **Q. WHAT IS YOUR EDUCATIONAL BACKGROUND?**

10 A. I received a Bachelor of Science degree from Weber State University in 1996 and a  
11 Masters of Business Administration from Utah State University in 2001.

12 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE UTAH PUBLIC SERVICE**  
13 **COMMISSION?**

14 A. Yes. I testified before the Commission as an expert witness in Docket Nos. 01-2383-01,  
15 02-2266-02, 02-049-82, 03-049-49, 03-049-50, and 05-053-01.

16 **II. SUMMARY**

17 **Q. PLEASE SUMMARIZE AND DESCRIBE THE PURPOSE OF YOUR**  
18 **TESTIMONY.**

19 A. On September 2, 2005 Carbon/Emery Telecom, (Carbon/Emery), pursuant to Utah  
20 Admin. Code R746-360 filed an application for an increase in the amount of Universal

21 Service Fund (“USF”) support. In Utah Code Annotated § 54-8b-15.6 the State  
22 Legislature indicated the fund would be designed to:

- 23 a. promote equitable cost recovery of basic telephone service through the imposition  
24 of just and reasonable rates for telecommunications access and usage; and
- 25 b. preserve and promote universal service within the state by ensuring that customers  
26 have access to affordable basic telephone service.

27 In R746-360 the Public Service Commission (“Commission”) established rules to  
28 achieve the direction given by the Legislature. One element of the USF is the  
29 determination of an Affordable Base Rate (“ABR”). My testimony will discuss the  
30 purpose and goals of the USF, the current ABR in Utah, and the need to increase the  
31 ABR. In addition I will discuss some policy considerations with the USF that the  
32 Commission needs to consider.

33 **III. TESTIMONY**

34 **Q. WHAT IS THE PURPOSE AND GOALS OF THE USF?**

35 A. In 1997 the State Legislature passed legislation indicating that a fund would be established  
36 to “promote equitable cost recovery of basic telephone service through the imposition of  
37 just and reasonable rates for telecommunications access and usage; and preserve and  
38 promote universal service within the state by ensuring that customers have access to  
39 affordable basic telephone service.”

40 On the Federal Level Universal Service has been a concept that has been implemented by  
41 the Federal Communications Commission (“FCC”) since 1934. With the passing of the  
42 1996 Telecommunications Act, Congress prescribed general principles on which the FCC

43 were “to base policies for the preservation and advancement of universal service.”<sup>1</sup>

- 44 • Quality services should be available at just, reasonable, and affordable rates;
- 45 • All regions of the nation should have access to advanced telecommunications and  
46 information services;
- 47 • Consumers throughout the nation, including low-income consumers and those in  
48 rural, insular, and high cost areas, should have access to telecommunications  
49 services that are reasonably comparable to those offered in urban areas at rates  
50 that are reasonably comparable to the rates charged in urban areas;

51 On both the Federal and State levels the goals of the USF are similar. The fund is to help  
52 establish a mechanism to equitably adjust the cost of service for high cost areas and provide  
53 affordable phone services in those high cost areas.

54 **Q. WHAT IS THE CURRENT AFFORDABLE BASE RATE FOR THE MAJORITY**  
55 **OF RURAL TELEPHONE CUSTOMERS IN UTAH?**

56 A. The current ABR has been approved for most rural telephone customers at \$13.50 for  
57 residential customers and \$23.50 for business customers.

58 **Q. HOW IS THE AFFORDABLE BASE RATE DEFINED AND USED IN THE**  
59 **STATE OF UTAH?**

60 A. Rule R746-360-2(A) defines the Affordable Base Rate as:

61 [T]he monthly per line retail rates, charges or fees for basic telecommunications service  
62 which the Commission determines to be just, reasonable, and affordable for a designated

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<sup>1</sup> 47 U.S.C. §254(b)(1)-(3).

63 support area. The Affordable Base Rate shall be established by the Commission. The  
64 Affordable Base Rate does not include the applicable USF retail surcharge, municipal  
65 franchise fees, taxes, and other incidental surcharges.

66 The ABR is used in determining the maximum price customers will pay for phone service.  
67 Telecommunication companies are not allowed to charge more than the ABR to customers,  
68 with any shortfall of prudent costs of a high cost area covered by the State USF.

69 **Q. WHEN WAS THE AFFORDABLE RATE ESTABLISHED BY THE**  
70 **COMMISSION?**

71 A. On April 30, 1999 in Docket No. 99-046-01 In the Matter of the Increase of Rates and  
72 Charges by Manti Telephone Co. and on July 3, 2000 in Docket No. 00-043-01 In the  
73 Matter of the Increase of Rates and Charges by Gunnison Telephone Company the  
74 Commission raised each company's rates to the \$13.50 and \$23.00 level for residential  
75 customers and business customers respectively. In the Manti Case the Commission  
76 approved rate increases of \$2.50 for residential customers and \$7.20 for business  
77 customers, while Gunnison was granted increases of \$2.50 for basic residential phone  
78 service and \$5.00 for basic business service.

79 **Q. IS CARBON/EMERY USING THIS AFFORDABLE RATE IN THIS DOCKET?**

80 A. Yes. Carbon/Emery has filed testimony with the Commission indicating that local  
81 rates be increased from \$11.03 and \$19.37 for residential and business customers to the  
82 \$13.50 and \$23.50 rates. This would be the first rate increase requested by Carbon/Emery  
83 since purchasing the exchanges from Qwest.

84 **Q. SINCE 1999 HAS THE COMMISSION INCREASED THE AFFORDABLE RATE?**

85 A. Over the last five or six years when other rural carriers have asked for USF increases, the  
86 Division has recommended that the companies' affordable rates be increased to the \$13.50  
87 and \$23.00. On November 4, 2005 the Commission issued an order in Docket No. 05-053-  
88 01 dealing with a rate increase for Uintah Basin Telephone. The Commission's order  
89 increased rates for Uintah Basin to \$16.50 and \$26.00 for residential and business  
90 customers.

91 **Q. IS THE DIVISION RECOMMENDING RAISING THE AFFORDABLE RATE IN**  
92 **THIS CASE?**

93 A. Yes. The Division is recommending raising the affordable rate in this case for basic  
94 residential service to \$16.50 and for basic business service to \$26.00, or an additional \$3  
95 increase for each class of customers from the proposed affordable base rate by  
96 Carbon/Emery.

97 **Q. IS THE DIVISION RECOMMENDING IMPLEMENTING THE ENTIRE RATE**  
98 **INCREASES WITH THIS DOCKET?**

99 A. No.

100 **Q. HOW IS THE DIVISION RECOMMENDING THE PROPOSED RATE**  
101 **INCREASES BE IMPLEMENTED?**

102 A. For a number of years Carbon/Emery customer's rates have been below the affordable base  
103 rate approved for most customers in Utah. To rectify this situation Carbon/Emery has  
104 proposed "increasing basic service from the current rates for basic service to \$13.50 and  
105 \$23.00 for, respectively, residence and business one-party service. These represent  
106 increases from the respective current tariffed rates of \$11.03 and \$19.37 of \$2.47 and \$3.63  
107 respectively." Division's revenue requirement examination shows that not all of the

108 requested increase is justified. The Division feels adding an additional three dollar increase  
109 to customers in addition to the increases suggested by Carbon/Emery would be imprudent  
110 and an undue burden to customers. Recognizing this situation the Division recommends  
111 that the Commission adopt a graduated approach in implementing the increases when they  
112 become cost justified

113 **Q. WHAT IS THE BASIS FOR THE DIVISION'S RECOMMENDING AN INCREASE**  
114 **IN THE AFFORDABLE RATE TO \$16.50 AND \$26.00?**

115 A. Because the term "affordable" is a very subjective term it is difficult to have an iron clad  
116 definition of what would be an acceptable level for the affordable rate. The Division feels  
117 the best way to determine the affordable rate would be to look at national and regional  
118 benchmarks and what other states have determined to be an acceptable affordable rate.  
119 Using this information the Division can compare Utah with other parts of the nation. With  
120 this comparison, the Commission will be able to see that the affordable rate recommended  
121 is reasonable compared to other states and reasonable for Carbon/Emery.

122 **Q. WHAT IS THE AVERAGE RATE FOR LOCAL SERVICE ON THE FEDERAL**  
123 **LEVEL?**

124 A. Every year the FCC publishes a study on telephone trends. On June 21, 2005 the FCC  
125 released the report showing the average rate for local service for residential service at  
126 \$14.53 and for business service \$32.81 as of October 15, 2004.

127 **Q. HOW ARE THE AVERAGE RATES CALCULATED BY THE FCC?**

128 A. For years the Bureau of Labor Statistics ("BLS") has collected a variety of information on  
129 telephone service as part of three separate programs the Consumer Price Index ("CPI"), the



130 Producer Price Index (“PPI”), and the Consumer Expenditure Survey.<sup>2</sup> The price indices  
131 maintained by the BLS indicate percentage changes in the price of telephone services. BLS  
132 does not publish actual rate levels. Calculations of average rates are based on surveys by  
133 FCC staff. These surveys use the same sampling areas and weights used by BLS in  
134 constructing the CPI. Using the information from the FCC surveys and the BLS  
135 information the average rates are calculated.

136 **Q. THE RATES PUBLISHED BY THE FCC ARE FOR URBAN AREAS. WHY DOES**  
137 **THE DIVISION FEEL THAT THESE RATES ARE APPLICABLE IN THIS CASE**  
138 **WHEN CARBON/EMERY IS A RURAL CARRIER?**

139 A. The Division feels there are at least two major points that can be drawn from the  
140 information provided on a national level from the FCC. The first bit of information is the  
141 ability to see general trends that is happening in the industry. The Division feels it is a  
142 plausible theory that phone rates in Carbon/Emery’s serving territory would probably be  
143 following the general trends in the industry, without government regulation. As attachment  
144 3.1 shows, the trendline for residential rates has generally been upward, especially if you  
145 look at the years from 1999 to 2004. From the year 2000 to 2001 there was a significant  
146 increase in residential rates. Because the affordable rates in Utah have not changed in the  
147 last five or six years, prices have not been adjusted to reflect that spike in rates that  
148 happened on the federal level.

149 Other information that can be gleaned from the data is what consumers generally feel is an  
150 “affordable” rate for phone service. Inherent in an average is the concept that there are  
151 rates that will be both higher and lower than the average. Because of this principle, the  
152 Division is able to determine that in urban areas consumers are paying rates that would be

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<sup>2</sup> The BLS Indices can be found at [www.bls.gov](http://www.bls.gov).

153 comparable to the proposed increases for this case; therefore if consumers in urban areas  
154 are choosing to purchase services, they are voting with their dollars that the rates must be  
155 affordable.

156 **Q. THE FEDERAL AVERAGE RATE FOR PHONE SERVICE IS \$14.53 AND \$32.81.**  
157 **WHY IS THE DIVISION RECOMMENDING AN INCREASE TO \$16.50 AND**  
158 **\$26.00?**

159 A. The reason the Division is recommending rates at the above mentioned levels comes back  
160 to the purpose of the Fund as stated by the Legislature. The Fund is to “promote equitable  
161 cost recovery of basic telephone service through the imposition of just and reasonable rates  
162 for telecommunications access and usage; and preserve and promote universal service  
163 within the state by ensuring that customers have access to affordable basic telephone  
164 service.” With Carbon/Emery requesting a substantial increase in revenues the Division  
165 feels that having all consumers, both Carbon/Emery customers as well as the other phone  
166 customers in the State of Utah, bearing the obligation for the increased revenues would be  
167 the most equitable way to recover the costs of Carbon/Emery. As stated before the federal  
168 rate is an average for urban customers. It is general knowledge in the telecommunications  
169 industry that rural customers’ rates are higher than urban customers’ rates. With this  
170 understanding that rural rates are generally higher than urban rates and customers in urban  
171 areas across the country are paying on average \$14.53, an increase in rates to \$16.50 for  
172 Carbon/Emery would be affordable. The Division also believes the increase to \$16.50 is  
173 justified, because of the revenue requirements of Carbon/Emery, as an equitable method to  
174 spread the revenue requirements among all customers of the state.

175 **Q. WHAT HAVE OTHER STATES SET AS THEIR AFFORDABLE RATE?**

176 A. The Division researched a variety of other states to see what was being done by those

177 Commissions with a state USF program. The Division found that North Dakota's state  
178 legislature has set the affordable rate at \$17.82, excluding surcharges and other additives,  
179 for residential customers. Oregon reports that its state commission established \$21.00 as  
180 affordable. In Colorado the average rate for rural customers is \$16.45. Wyoming uses a  
181 support benchmark that changes every year. For 2005 the Wyoming benchmark amount  
182 was established at \$31.80.

183 **Q. OF ALL THE STATES LISTED ABOVE DO YOU THINK ONE IS A BETTER**  
184 **REPRESENTATION OF UTAH THEN THE OTHERS?**

185 A. Yes. The Division feels that Colorado is probably the state that would be most comparable  
186 to Utah. Colorado has a similar situation in that Qwest is the major phone company with a  
187 number of rural phone carriers serving in the state as well. It is reasonable to believe that  
188 rural Colorado would not differ much from rural Utah. The Division contacted Colorado to  
189 determine how their state handles rural carriers. Staff from Colorado provided a  
190 spreadsheet<sup>3</sup> that tracked the rural rate charged in Colorado from 1983 to 2003. The  
191 information shows that the rates proposed by the Division are similar to the average rate  
192 calculated by the Colorado Commission. Another interesting point with the data provided  
193 is that the trend in Colorado for basic phone service is similar to the trend on the Federal  
194 Level. Over the past 20 years or so rates have followed an upward trend on both residential  
195 and business services.

196 **Q. ARE THERE OTHER POLICY ISSUES YOU THINK THE COMMISSION**  
197 **SHOULD CONSIDER WITH USF AND CARBON/EMERY'S APPLICATION?**

198 A. Yes. There are some general policy considerations that the Commission should consider

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<sup>3</sup> See Attachment 3.3 for Residential rates and 3.4 for Business rates.

199 with USF. One of those items is the apparent disconnect between the revenues of a  
200 company and the underlying costs of a regulated entity when USF can be used. Any basic  
201 accounting or finance textbook would include the simple equation that Revenues –  
202 Expenses = Net Income (or Net Loss).

203 In a normal competitive market any business must look at the price they are going to  
204 charge its customers against the costs of providing that service. Because of market forces  
205 and competitive pressures, generally a company will either look for ways to increase  
206 revenues through a higher selling price of the goods or developing a way to offer the  
207 service at a lower cost. If McDonalds wants to make more money selling Big Mac  
208 hamburgers, assuming constant volumes, then they either have to convince consumers that  
209 their Big Mac is worth paying a higher amount for, or another alternative would be to  
210 develop a way to control the costs of producing the Big Mac.

211 In a regulatory environment the market constraints that would force either cost reductions  
212 or allow for higher prices are restrained. In Utah, rate of return regulated companies are  
213 allowed to get a certain level of revenues from a combination of the prices charged  
214 customers and revenues from the USF. Looking at the basic equation given above, because  
215 of the regulatory regime in place in Utah, there is no practical restraint on the revenue. If  
216 prices charged by a company that is rate of return regulated do not cover the costs of the  
217 company then the USF would be required to make up the difference.

218 The Division recognizes that the “price” a rate or return regulated company can charge is  
219 not in the control of that company, but something that definitely is in the control of any rate  
220 or return regulated company is its costs. The Division understands that the purpose of the  
221 USF is to help prudently managed companies in high cost areas provide affordable phone  
222 service to the individuals living in that area and wholeheartedly supports use of USF funds

223 to further this purpose. At a fundamental level though, the Division recognizes that  
224 underlying costs of a company define price. The Commission may have considerable  
225 power to spread those costs across both services and consumers, but ultimately the cost of  
226 service will define the price or revenues needed by the company under the legislature's  
227 stated USF policy.

228 Recently, it appears, the Commission has followed a general policy of charging the same  
229 affordable rate for all of the rural companies in the State. The uneasiness of the Division  
230 with using the same affordable rate for every company is that there is no incentive for a  
231 company to really look at costs and to be as efficient as possible. Using the same rate for  
232 all companies means that customers of an efficient high cost company and an inefficient  
233 high cost provider would be paying the same rate. To overcome this disconnect between  
234 revenues and costs the Division would recommend looking at using a range of affordable  
235 rates specific to the situation and needs of the requesting company. Customers of an  
236 inefficient company may end up with a marginally higher rate than an efficient high cost  
237 company because the costs or service are vastly different.

238 The Division firmly believes that the best way the Commission can provide an incentive  
239 for utility management to be efficient is to have some of the "costs" of the company trickle  
240 back to the company's customers. If any telecommunications company, barber shop,  
241 information technology company, etc. knew that it was going to have to ask customers to  
242 pay a little more for its service, I believe those companies would make sure they have done  
243 everything in their power to reduce unnecessary expenses or hopefully even eliminate  
244 spurious costs.

245 **Q. WHAT IS THE DIVISION'S UNDERSTANDING OF THE COMPETITIVE**  
246 **IMPACT OF RAISING RATES?**

247 A. The Division does not believe that there will be a significant migration of customers from  
248 Carbon/Emery to a competitor because of the rate increases. Currently Carbon/Emery is  
249 the only company that has authority to offer land-line services. Because of this fact  
250 consumers would have to choose to change from their wireline phone to a wireless phone  
251 product. Although the wireless market is growing and improving with technology, the  
252 Division has not found any data or studies that convincingly prove that there is a huge  
253 wave of customers that replace wireline phones with wireless. Because of the lack of a  
254 variety of options to replace wireline service in the Carbon/Emery serving areas, the  
255 Division believes few if any customers are going to switch phone service with the changes.  
256

257 **IV. CONCLUSION**

258 **Q. WHAT IS THE DIVISIONS RECOMMENDATION WITH THIS PETITION?**

259 A. The Division recommends raising Carbon/Emery's Affordable rate to \$16.50 for residential  
260 customers and \$26.00 for business customers with a gradual increase of the rates over the  
261 next few years as the company's costs justify additional rate increases. The Division also  
262 recommends using a gradual approach to increasing the rates of customers and that  
263 Carbon/Emery should not be authorized to obtain state high cost fund USF support until the  
264 costs of service exceeds the recommended affordable base rate.

265 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

266 A. Yes it does.